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File Number: S7-10-22
The Enhancement and Standardization of Climate-Related Disclosures for Investors

Dear Ms. Countryman:

"Hamlet Without the Prince"

In his recent memoir, *One Damn Thing After Another*, former attorney general William Barr wrote of the legal challenge to the proposed citizenship question that the Commerce Department and its secretary, Wilbur Ross, had wanted in the 2020 census:

> In January 2019 a federal district court in Manhattan found that Ross's decision violated the Administrative Procedure Act because Commerce's declared rationale for asking the citizenship question was pretextual—that is, it was not the real reason behind the decision.[1]

After the Trump administration lost its appeal in the Supreme Court, Barr briefed President Trump on the outcome:

> "I agree we should be able to ask the question," I started. "And if people were straightforward from the beginning, it could have gotten done. The trouble is the administration was too cute by half, and [Chief Justice John] Roberts threw the penalty flag."[2]

The purpose of this comment letter is to examine whether the declared rationale of the Securities and Exchange Commission (the "SEC") for its recently proposed rulemaking on climate-related disclosures (the "Proposal") is genuine, rational, and logical, or whether it is, as was the case with the Commerce Department's proposed citizenship question in the 2020 census, pretextual. The letter demonstrates that the Proposal, especially with regard to compelled disclosures of greenhouse gas ("GHG") emissions, makes sense only in terms of meeting an undisclosed rationale—indeed, one that the SEC explicitly denies having. "Thus," it states with respect to Scope 3 GHG emissions (those emitted by third parties from across a firm's entire value chain),

[1] William P. Barr, *One Damn Thing After Another: Memoirs of an Attorney General* (New York: William Morrow, 2022), p. 274.
[2] Ibid., p. 277.

> the objective of this disclosure is not to drive targets, goals, plans, or conduct, but to provide investors with the tools to assess the implications of any targets, goals, or plans on the registrant in making investment or voting decisions.[3]

In her dissenting remarks on the day the Proposal was published, SEC Commissioner Hester Peirce declared:

> Let us be honest what this proposal is really trying to do. Although styled as a disclosure rule, the goal of this proposal—as with other climate disclosure efforts—is to direct capital to favored businesses and to advance favored political and social goals.[4]

It is not possible for both these comments to be right. It is binary: either the SEC is right and Commissioner Peirce is wrong; or the SEC is wrong and Commissioner Peirce is right.

Much commentary on the Proposal centers on whether the SEC has the statutory authority to, in effect, regulate GHG emissions. If the SEC believed that it had the authority to do so, the question of pretextuality—in plain English, the stated justification is a pretext for something else—would not arise. The two issues are linked. Determining whether the SEC's public rationale for the Proposal is pretextual also sheds light on whether the SEC is likely to exceed its authority, were it to adopt disclosure rules set out in the Proposal.

Moreover, language in the Proposal that could be interpreted as the SEC attempting to avoid the pretextual trap has implications that are fatal for much of the Proposal. Much of the stated justification for the Proposal is in response to investor demand for mandated disclosures. Yet the strategy adopted by the SEC to justify the Proposal precludes the SEC from admitting that GHG disclosures are useful to investors in imposing, monitoring and enforcing GHG reduction targets on investee companies. Instead, it concedes that meeting GHG reduction targets can be costly, which, in turn, leads the SEC to downplay investor demand for GHG disclosures' use as a tool to force companies to cut their GHG emissions.

If meeting GHG reduction targets has negative implications for shareholder value, it implies that investors wanting such information as part of an effort to press for, and monitor, such targets are not acting in the economic interests of shareholders but in furtherance of some other, noneconomic motive. Were the SEC to hang its hat on its denial that GHG disclosure requirements are designed to drive decarbonization targets and goals—that is to say, its claim that the aim of the Proposal is *not* to facilitate the setting and monitoring of GHG reduction targets, then much of the investor demand for climate disclosures cited in the Proposal must be discarded because their demands are not motivated by shareholder return considerations, thus necessitating fundamental changes to the substance of the Proposal to align it with the residual of its non-pretextual rationale.

The arguments in this comment letter are organized in six principal sections, the first four of which demonstrate that the SEC's underlying justification for the Proposal is not its stated one—i.e., the rationale is pretextual.

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[3] The Proposal, p. 178.

[4] SEC, Hester M. Peirce, "We Are Not the Securities and Environment Commission—at Least Not Yet" (Mar. 21, 2022), fn. 61, https://www.sec.gov/news/statement/peirce-climate-disclosure-20220321.

First, the SEC presents no conclusive evidence as to the inadequacy of existing materiality disclosure rules and its current guidance regarding disclosure of material climate change risks and impacts published in 2010 to justify the Proposal's new disclosure framework.[5] Indeed, some of the commentary contained in the Proposal is convoluted, inconsistent, and, in one place, the evidence it cites contradicts what the SEC claims.

Second, the SEC proposes adoption of a GHG disclosure regime designed to facilitate investors and other actors imposing and monitoring decarbonization targets on businesses; yet the SEC would have us believe that this is a coincidence and arises for reasons of administrative convenience because foreign jurisdictions require similar disclosures. Similarly, we are implicitly asked to believe that it is a coincidence that the Proposal conforms with a presidential Executive Order on adoption of a whole-of-government approach to climate financial risk disclosure.

Third, the SEC concedes that meeting GHG reduction targets could damage firms' productivity, raise costs, and lower profitability and thereby negatively affect shareholder interests. Nonetheless, it proposes to impose a rigid climate disclosure regime at the behest of certain investors and climate activists, but fails to ask "Why?" This failure puts question marks over the credibility of the SEC's denial that its purpose in compelling GHG emissions disclosures is to drive adoption and monitoring of corporate decarbonization targets; and over the Proposal's reliance on investor representations in favor of GHG disclosures.

Fourth, with respect to climate transition risk arising from regulatory and other governmental climate policy interventions, corporate GHG disclosures are a systematically misleading indicator of such risk because they falsely assume that the world is a homogenous regulatory space. The lack of jurisdictional contiguity between corporate decarbonization programs and actual governmental climate policies has major implications for the likely costs of the Proposal, which are completely neglected in the Proposal's superficial and cursory cost-benefit analysis.

Fifth, the nebulous nature of climate financial risk, evidenced by some of the errors and misconceptions that the SEC commits in the Proposal, means that the Proposal's highly prescriptive approach is not warranted, if the SEC is genuine in its declared aim of seeking to improve investor understanding.

Sixth, in light of the foregoing and shorn of its pretextual provisions, this letter suggests elements of the Proposal that could be retained as useful additions to the SEC's 2010 guidance, in order to reflect subsequent developments and improve the hygiene of climate and ESG reporting and, therefore, investor understanding.

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This letter is organized as follows:

I. Lack of an Evidence-Based Justification for the Proposal
II. GHG Disclosures as Corporate Decarbonization Tool—Coincidence or Evidence of Undisclosed Intent?
    A. Genesis and Context of the Proposal

[5] SEC, "Commission Guidance Regarding Disclosure Related to Climate Change" (Feb. 2010), https://www.sec.gov/rules/interp/2010/33-9106.pdf.

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I. Lack of an Evidence-Based Justification for the Proposal

If the justification for the Proposal is genuine and not pretextual, it is reasonable to expect that the SEC would provide evidence and analysis demonstrating that the current framework—in particular, the SEC’s 2010 interpretative guidance—has failed and that a significant number of registrants have not disclosed material facts and risks related to climate change. Instead, the reasoning and evidence base is thin and, at times, contradicts the case that the SEC is trying to make.

The Proposal notes that the current disclosure framework relies, to an extent, on management judgment as to what is material but does not cite evidence that indicates registrants failing to discharge their disclosure obligations.[6] On the contrary, it finds that the proportion of Russell 3000 firms providing climate-related disclosures in their 10-K filings nearly doubled in 11 years, rising from 35% of the Russell 3000 in 2009 to 60% in 2020.[7] The SEC plays something of a shell game when it argues that voluntary disclosures are not sufficient, by switching from the materiality standard that underpins the current principles-based mandatory disclosure framework to a relevant information standard. Agency problems, the SEC argues, may result in managers withholding relevant information.

> In contrast, when the disclosure requirements are mandatory, the relevant, complete information should be disclosed regardless of managers’ objectives or incentives.[8]

Here we have the SEC implicitly conceding that the information covered by its proposed disclosure rules does not meet the materiality standard of federal securities law and “relevant to what?” is a question the Proposal neither poses or answers.

[6] The Proposal, p. 309.
[7] The Proposal, p. 324.
[8] The Proposal, p. 340.

In the absence of hard data to support its case, much of the Proposal's economic justification consists of abstract theorizing. The SEC acknowledges that existing accounting standards could elicit climate-related disclosure.

> Nevertheless, we believe the proposed rules would benefit registrants by specifying when to provide such disclosures.[9]

Are we to believe that the purpose of the proposed rules is merely to specify the timing of climate-related disclosures? Elsewhere, the Proposal states that although current accounting standards require disclosure of information as to how climate-related matters intersect with and affect the financial statements,

> the nature of the climate-related events and transition activities discussed in the proposed rules, which may manifest over a longer time horizon, necessitate targeted disclosure requirements to elicit decision-useful information for investors in a consistent manner.[10]

What does this actually mean? Is the SEC saying that existing accounting standards with respect to climate disclosures are applied in an inconsistent manner? What is it about the specific nature of climate risks that necessitates additional disclosures over and above those already required by accounting standards? Instead of providing any answers, the SEC serves up verbal blancmange. "Prior evidence," the Proposal asserts,

> shows that existing climate-related disclosures often contain boilerplate language or are "cherry-picked" to present information that is favorable to the company.[11]

The purported evidence cited is two papers.[12] The first is a December 2021 paper, "Cheap Talk and Cherry-Picking," by four German and Swiss academics ("Bingler et al.").[13] Of the 818 company disclosures analyzed in the paper, only 15.01% are from North America.[14] Worse still for the Proposal, the paper shows the opposite of what the SEC contends. The Proposal is modeled on the Task Force on Climate-related Financial Disclosures ("TCFD") framework, and Bingler et al. is designed to assess the effect on disclosures of companies adopting the TCFD framework. Disappointingly for the SEC, the authors' results

> show that supporting the TCFD seems to be cheap talk and is associated with cherry-picking disclosures on those TCFD categories containing the least materially relevant information.[15]

Bingler et al. find "only a slight or negligible" increase in information disclosed as required by TCFD categories. Still more damning for the Proposal is the authors' conclusion that

> much of the information has already been disclosed before the launch of the TCFD recommendations. This observation, which is left out of the TCFD status report, suggests that TCFD-supporting firms might not have increased their

[9] The Proposal, p. 117.
[10] The Proposal, p. 148.
[11] The Proposal, p. 366.
[12] The Proposal, fn. 870.
[13] The Proposal, fn. 829.
[14] Julia Anna Bingler et al., "Cheap Talk and Cherry-Picking: What ClimateBert Has to Say on Corporate Climate Risk Disclosures," *Finance Research Letters* (Feb. 25, 2022), table 4.
[15] Ibid., p. 2.

> level of disclosures. Instead, they might simply have re-structured already existing information such that they comply with TCFD recommendations.[16]

The second citation is not a research paper like Bingler et al. but a policy paper by the board of the International Organization of Securities Commissions ("IOSCO"), of which the SEC is a member and Chair Gary Gensler is on its board.[17] Its first sentence reads:

> The financial sector has a crucial role to play in helping support the transition to a more sustainable future.[18]

- *It is the contention of this letter that this objective, as enunciated in the June 2021 IOSCO paper, better fits the purpose of the Proposal's provisions than the SEC's stated reasons.*

II. GHG Disclosures as Corporate Decarbonization Tool—Coincidence or Evidence of Undisclosed Intent?

As noted above, the SEC denies that the intent behind the Proposal's mandating disclosure of GHG emissions data is to encourage adoption and enforcement of GHG reduction targets. Rather, such disclosures could alert investors that "the registrant may need to make a large expenditure or significant change to its business operations."[19] A similar point is made 181 pages later: "[I]nvestors may gain better insights into the registrant's estimated costs of any operational changes expected to be implemented to achieve emission reduction targets."[20]

For such a densely footnoted text—in the Proposal's 438 pages of explanatory text, there are 1,005 footnotes, an average of 2.3 footnotes per page—the pages containing rare negative comments about GHG emissions targets on shareholder value are notably bereft of any references to letters from investors concerned about their implications on shareholder value. By contrast, in two pages in the Proposal's section "The Growing Demand for Climate-Related Risk Disclosure and Related Information," there are references to five investor groups. Not a single one evinces concern about the possible costs to businesses and shareholders of meeting corporate GHG emissions targets. As shown in Table 1 below, the cited documents and/or websites all contain statements emphasizing the role of investors in climate policy, and the Investor Agenda's 2021 statement highlights the critical role of government policies to increase climate-related disclosures to accelerate action on tackling the climate crisis.

[16] Ibid., p. 4.
[17] The Proposal, fn. 806.
[18] IOSCO, "Report on Sustainability-Related Issuer Disclosures: Final Report," June 2021, p. 1.
[19] The Proposal, p. 177.
[20] The Proposal, p. 358.

Table 1: Investor Citations on pp. 26–27 of the Proposal

Ref	Organization	Statement
57	Investor Agenda's Global Investor Statement to Governments on Climate Change—2019	▪ "The Investor Agenda provides an unprecedented global forum for investors to accelerate action on climate change and drive transformation of capital markets to deliver a 1.5-degree Celsius economy." ▪ "The Investor Agenda has a critical role to play in compelling investors to act and bring about lasting change around climate." ▪ "There is a growing urgency for investors and corporations to act on climate change goals."[21]
58	Investor Agenda's 2021 Global Investor Statement to Governments on the Climate Crisis	▪ "We stand at the beginning of a pivotal decade in which institutional investors and government leaders worldwide have the power to raise ambition and accelerate action to tackle the climate crisis." ▪ "Investors are taking climate action in line with the Investor Agenda, with more investors than ever before embedding net zero goals and strategies into their portfolio decisions." ▪ "[A]s owners of (or those representing owners of) companies, we need access to adequate information on how these companies are assessing and managing the risks and opportunities presented by climate change. Government policy has a critical role to play in increasing our access to and affirmative disclosure of such information."[22]
59	UN Principles for Responsible Investing	▪ "Now is the time for action: we're ready, our signatories are ready and the world's people deserve a response."—Fiona Reynolds, PRI Managing Director[23]
61	Net Zero Asset Managers initiative	▪ "The Net Zero Asset Managers initiative is an international group of asset managers committed to supporting the goal of net zero greenhouse gas emissions by 2050 or sooner, in line with global efforts to limit warming to 1.5 degrees Celsius; and to supporting investing aligned with net zero emissions by 2050 or sooner."[24]

[21] United Nations Framework Convention of Climate Change (UNFCCC), "631 Institutional Investors Managing More than USD 37 Trillion in Assets Urge Governments to Step Up Climate Ambition," Dec. 9, 2019, https://unfccc.int/news/631-institutional-investors-managing-more-than-usd-37-trillion-in-assets-urge-governments-to-step-up.

[22] Investor Agenda, "2021 Global Investor Statement to Governments on the Climate Crisis," Oct. 27, 2021, https://theinvestoragenda.org/wp-content/uploads/2021/09/2021-Global-Investor-Statement-to-Governments-on-the-Climate-Crisis.pdf.

[23] UN PRI, "A Blueprint for Responsible Investing," https://www.unpri.org/about-us/a-blueprint-for-responsible-investment.

[24] https://www.netzeroassetmanagers.org.

Ref	Organization	Statement
62	Climate Action 100+	▪ "Climate Action 100+ is an investor-led initiative to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change."[25]
63	Glasgow Financial Alliance for Net Zero	▪ "We're focused on broadening, deepening and raising net-zero ambitions across the financial system and demonstrating firms' collective commitments to supporting companies and countries to achieve the goals of the Paris Agreement. We also support collaboration on steps firms need to take to align with a net-zero future."[26]

[25] https://www.climateaction100.org/about.

[26] https://www.gfanzero.com/about.

Elsewhere in the Proposal, the SEC is more forthcoming about the function of compulsory GHG emissions disclosures in decarbonizing investor portfolios, which undercuts the SEC's denial that mandatory disclosures are about driving targets and goals. It notes that several large institutional investors have made commitments to achieve a net-zero economy by 2050 and interim targets set for 2030:

> These investors and financial institutions are working to reduce the GHG emissions of companies in their portfolios or of their counterparties and need GHG emissions data to evaluate the progress made regarding their net-zero commitments.[27]

This accords with data for the 2022 proxy season. As of March 2022, 529 shareholder resolutions had been filed on environmental, social, and related sustainable governance issues for the 2022 proxy season, up more than 20% from last year at that time.[28] The number of proposals specifically on climate change had risen to a record 110 (up from 79 last year). "A striking change is the near-total focus on greenhouse gas (GHG) emissions targets, with most proposals asking for a transition to net-zero status by 2050," the authors of *Proxy Preview 2022* note.[29] By contrast, there is no record of any resolutions being filed requiring companies to disclose the costs of meeting corporate net-zero targets.[30]

The SEC asks how investors would use GHG disclosures to inform their investment and voting decisions (Question 93).

- *All the available evidence indicates that SEC-compelled GHG emissions disclosures would be used by large institutional shareholders and climate activists to monitor, impose, or tighten corporate GHG reduction targets.*

- *Other than the SEC's assertions noted above, there is no evidence of investors wanting mandatory GHG emissions disclosures in order to assess the cost and other business implications of meeting GHG emissions reduction targets. Indeed, it would be illogical for the SEC to impose GHG emissions disclosure requirements on the grounds that it would enable investors to assess the costs of meeting GHG reduction targets derived from such disclosures. The circular reasoning is as obvious as it would be irrational.*

A. Genesis and Context of the Proposal

Many of the investor letters cited in the Proposal were submitted to the SEC in response to a call for comments to inform a review of climate disclosures launched in March 2021 by the SEC's acting chair, Allison Herren Lee, which trailed mandatory Scope 1–3 GHG emissions disclosures. This subsection examines the genesis of the Proposal and the wider policy context in which it was formulated and demonstrates the implausibility of the SEC's denial of any pretextual motive behind the Proposal.

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[27] The Proposal, p. 166. This passage cites Climate Action 100+ and Glasgow Financial Alliance for Net Zero (GFANZ).

[28] Heidi Welsh & Michael Passoff, *Proxy Preview 2022*, p. 5.

[29] Ibid., p. 6.

[30] Proposals requiring audited reports on changes to the assumptions, costs, and valuations from applying the International Energy Agency's (the "IEA") net-zero pathway have been submitted to three oil companies. These are not, however, about the costs of meeting corporate GHG reduction targets but about the IEA's assumption of falling oil prices and there being no need for new investment in oil and gas production. Ibid., p. 27.

In her speech announcing the review, the SEC acting chair articulated the link between investor disclosures and investor action. "Human capital, human rights, climate change—these issues are fundamental to our markets, and investors want to and can help drive sustainable solutions on these issues."

> That's why climate and ESG are front and center for the SEC. We understand these issues are key to investors—and therefore key to our core mission. And just as we recognize that these issues do not observe artificial distinctions between society and financial markets, we recognize that climate and ESG transcend other boundaries as well. Geographical boundaries for one. These are global challenges for global markets that demand global solutions. Regulatory boundaries for another. Climate, for instance, is not just an EPA, Treasury, or SEC issue—it's a challenge for our entire financial system and economy.[31]

The SEC review took place against a backdrop of the countdown to the United Nations COP26 climate conference in Glasgow in November 2021. Five weeks after the launch of the review, Mark Carney, the UN Special Envoy on Climate Action and Finance, announced the formation of the Glasgow Financial Alliance for Net Zero (GFANZ), with the aim of building a global net-zero economy (see Table 2 for a detailed chronology). GFANZ is cited three times in the Proposal. Of the top seven investors cited in the Proposal, five (BNP Paribas, BlackRock, Impax Asset Management, Baillie Gifford, and Trillium Socially Responsible Investment) are members of GFANZ's Net Zero Asset Managers initiative, for a total of 50 footnote citations in the Proposal.[32] These are asset managers that have publicly committed to:

- Support the goal of net-zero GHG emissions by 2050;
- Take account of portfolio Scope 1 and 2 emissions and, to the extent possible, material portfolio Scope 3 emissions; and
- Prioritize the achievement of real economy emissions reductions within the sectors and companies in which they invest.[33]

[31] SEC, "A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC," speech by Acting Chair Allison Herren Lee, Mar. 15, 2021, https://www.sec.gov/news/speech/lee-climate-change.
[32] https://www.netzeroassetmanagers.org/signatories.
[33] https://www.netzeroassetmanagers.org/commitment.

Table 2: Chronology of Key Events

Jan. 21, 2021	▪ President Biden appoints Allison Herren Lee acting chair of the SEC
Mar. 15, 2021	▪ Acting Chair Lee launches review to evaluate whether existing rules facilitate "the disclosure of consistent, comparable, and reliable information on climate change"[34] ▪ Trails mandatory disclosure of Scope 1–3 GHG emissions data
Apr. 17, 2021	▪ Gary Gensler sworn in as SEC chair
Apr. 21, 2021	▪ Mark Carney launches the Glasgow Financial Alliance for Net Zero (GFANZ), with more than 160 firms with combined assets under management of over $70 trillion ▪ "GFANZ will work to mobilise the trillions of dollars necessary to build a global zero emissions economy and deliver the goals of the Paris Agreement"[35]
May 20, 2021	▪ President Biden issues Executive Order on Climate-Related Financial Risk ▪ Requires an assessment of climate-related financial risk by financial regulators ▪ As chair of the Financial Stability Oversight Council (FSOC), Secretary of the Treasury required to submit report to the president within 180 days
June 5, 2021	▪ Virtual G7 meeting of finance ministers and central bank governors ▪ "We commit to a multi-year effort to deliver the very significant structural change needed to meet our net zero commitments"[36]
June 14, 2021	▪ Deadline for comments on evaluation of existing SEC climate disclosure framework
Oct. 21, 2021	▪ FSOC Report on Climate-Related Financial Risk recommends FSOC members review existing disclosure requirements and update them as appropriate, to "promote the consistency, comparability, and decision-usefulness of information on climate-related risks and opportunities, consistent with their mandates and authorities"[37]
Oct. 31–Nov 12, 2021	▪ Glasgow COP26 UN climate conference ▪ "Only mainstream finance can fund the estimated $100 trillion of investment needed over the course of the next three decades for a clean energy future"—Mark Carney[38]
Mar. 21, 2022	▪ SEC releases the Proposal

[34] SEC, Allison Herren Lee, "Public Input Welcomed on Climate Change Disclosures," Mar. 15, 2021, https://www.sec.gov/news/public-statement/lee-climate-change-disclosures.
[35] United Nations Environment Programme (UNEP), "Mark Carney, UN Race to Zero Campaign, COP26 Presidency Launch Net Zero Financial Alliance," Apr. 21, 2021, https://www.unep.org/news-and-stories/press-release/mark-carney-un-race-zero-campaign-cop26-presidency-launch-net-zero.
[36] HM Treasury, "G7 Finance Ministers and Central Bank Governors Communiqué," June 5, 2021, https://www.gov.uk/government/publications/g7-finance-ministers-meeting-june-2021-communique/g7-finance-ministers-and-central-bank-governors-communique.
[37] Financial Stability Oversight Council (FSOC), "Report on Climate-Related Financial Risk 2021" (Oct. 2021), p. 7.
[38] YouTube, "Mark Carney COP26, Nov. 4, 2021," https://www.youtube.com/watch?v=SwNauib2YGw.

Nine weeks after the launch of the SEC climate disclosure review, President Biden signed an Executive Order on Climate-Related Financial Risk (the "EO"), which declares it administration policy to advance "consistent, clear, intelligible, comparable and accurate" disclosure of climate-related financial risk in order to, inter alia, achieve the administration's target of a net-zero economy by 2050.[39] The EO required the Treasury secretary, as chair of the Financial Stability Oversight Council (the "FSOC"), to engage with FSOC members, who include the chair of the SEC, and report on their efforts to integrate consideration of climate-related financial risk in their policies and programs, and report back to the president.

Published ten days before the start of the Glasgow climate conference, the FSOC report recommended that FSOC members

> review their existing public disclosure requirements and consider, as appropriate, updating them to promote the consistency, comparability, and decision-usefulness of information on climate-related risks and opportunities.[40]

The FSOC noted that SEC staff were working on a proposal on disclosure requirements for public issuers and said that it was "encouraged" by the SEC's work on "this critical issue."[41] That encouragement reinforced the message from the June 5 virtual meeting of G7 finance ministers, when Treasury secretary Janet Yellen put her name to a communiqué emphasizing the need "to green the financial system" to help mobilize the trillions of dollars needed to meet national net-zero commitments. On the finance ministers' commitment to embed climate change and biodiversity loss into economic and financial decisions, the communiqué said:

> We support moving towards mandatory climate-related financial disclosures that provide consistent and decision-useful information for market participants and that are based on the Task Force on Climate-related Financial Disclosures (TCFD) framework…. We therefore agree on the need for a baseline global reporting standard for sustainability, which jurisdictions can further supplement.[42]

(Note the G7 finance ministers' commitment to implementing a sustainability accounting framework, which is discussed in subsection B below.)

- *For the SEC's assertion that the purpose of GHG emissions disclosures is not to drive emissions targets, goals, or conduct to be genuine, it is necessary to believe that the following have no influence on, or are not reflected in, the substantive provisions in the Proposal:*
  - *Acting Chair Lee's statement when she initiated the evaluation of current disclosure requirements about climate being "front and center" for the SEC because investors want to "help drive" solutions;*
  - *Letters submitted by investors, investor groups, and climate activists in response to the SEC's March 2021 evaluation; and*
  - *The October 2021 FSOC report, written in response to the May 20, 2021 EO, which expressly links climate financial risk disclosure with the achievement*

[39] The White House, "Executive Order on Climate-Related Financial Risk," May 20, 2021, https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk.
[40] FSOC, "Report on Climate-Related Financial Risk 2021" (Oct 2021), p. 7.
[41] Ibid.
[42] HM Treasury, "G7 Finance Ministers and Central Bank Governors Communiqué."

of the administration's 2050 net-zero emissions goal, along with its statement that it was "encouraged" by the SEC's progress on the Proposal.

In other words, it requires ignoring the evidence.

B. Importation of Foreign Jurisdictions' Policies and Disclosure Standards

In its discussion of the direct costs of mandatory GHG emissions disclosures, the Proposal notes that the required information overlaps with what a U.S. multinational financial institution already discloses under the EU's Prospectus Regulation.[43] "Failure to implement the proposed rules could lead to an informational gap between U.S. registrants and companies operating in foreign jurisdictions which require climate-related disclosures," the SEC warns.[44]

> Lack of standardized disclosures around Scope 1 and 2 GHG emission by U.S. companies … may obstruct foreign counterparts from accurately assessing their Scope 3 GHG emissions, thus putting U.S. registrants at a competitive disadvantage over other foreign companies which may be publically [sic] disclosing such information.[45]

This might be called the "others are doing it, so we must" justification, which, if adopted as a principle of financial regulation and reporting standards, could have wider applicability than to the disclosure rules under consideration in the Proposal. If this justification were to become embedded, it would elevate the European Commission as the de facto disclosure standard-setter for the U.S., even though the U.S. has not adopted or legislated anything approaching the EU's corporate financial sustainability framework.

In March 2018, the European Commission published its action plan for financing sustainable growth, with the objective of reorienting capital flows to a more sustainable economy. In the words of a recital to the June 2020 Taxonomy Regulation for climate mitigation regulation:

> Sustainability and the transition to a safe, climate-neutral, climate-resilient, more resource-efficient and circular economy are crucial to ensuring the long-term competitiveness of the Union economy. Sustainability has long been central to the Union project, and the Treaty on European Union and the Treaty on the Functioning of the European Union (TFEU) reflect its social and environmental dimensions.[46]

Other EU legislation to further this policy objective include the Taxonomy Regulation, the Sustainable Finance Disclosure Regulation, and the EU Low Climate Benchmark Regulation, plus a proposal for a Corporate Sustainability Reporting Directive. These will see investment institutions reporting the carbon footprint of their portfolios and sustainability standards, incorporating the disclosure recommendations of the Task Force on Climate-related Financial Disclosures, on larger companies.

The SEC notes that several foreign jurisdictions are already incorporating TCFD disclosure recommendations into their legal and regulatory frameworks.[47] Such disclosures,

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[43] The Proposal, p. 393.
[44] The Proposal, p. 417.
[45] Ibid.
[46] Official journal of the European Union, "Regulation (Eu) 2020/852 of the European Parliament and of the Council of 18 June 2020," https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32020R0852.
[47] The Proposal, fn. 95.

the SEC argues, could assist investors in understanding the "overall risk"—the SEC uses "risk" where the EU talks of "sustainability"—of their portfolios, thus transitioning an EU policy objective into SEC disclosure regulation.[48] If allowed to stand, this could create a consequential precedent. It would be the de facto financial regulation equivalent of the Clean Air Act's California waiver, under which California's more stringent regulation of auto tailpipe emissions sets emissions standards adopted by other states. As indicated by the June 2021 G7 finance ministers, mandatory GHG disclosures are just the start. Next down the pike are biodiversity loss and reporting standards on sustainability.[49]

- *By signing the June 2021 G7 finance ministers' communiqué, the Biden administration signaled its intention to adopt a global reporting standard for sustainability. Were the SEC's "administrative convenience" justification for this Proposal allowed to stand, it would provide a backdoor route to transposing EU-style sustainability, social, and circular economy policies for business into the U.S., without the approval of Congress.*

III. GHG Reduction Targets, Shareholder Value, and Investor Motivation

The SEC's justification for the Proposal relies heavily on investor demand for mandatory disclosures along the lines of the TCFD reporting framework, but does not examine why. Evidence omitted from the Proposal shows that such investors are strongly motivated by the desire to impose GHG emissions reduction targets on companies, a goal that the leadership of the TCFD says that adoption of the TCFD framework would facilitate. But the Proposal's denial that the purpose of emissions disclosures is to drive GHG target-setting puts this explanation out of bounds.

By conceding that investor-imposed emissions cuts could be detrimental to shareholder value, the SEC implicitly accepts Commissioner Peirce's argument that investor representations in favor of GHG disclosures should be discounted because they are not motivated by an interest in financial returns from an investment in a particular company, but by deep concerns about the climate.[50]

A. TCFD and Corporate Decarbonization Targets

In proposing adoption of much of the TCFD framework, the SEC notes that many commenters advocated it as a basis for the Proposal on the grounds that: i) it is already in widespread use; ii) it elicits useful information; and iii) various jurisdictions are aligning their disclosure rules with it.[51] However, the Proposal omits crucial information on the underlying purpose of the TCFD and the likely use of the disclosures that it would elicit in a manner that fundamentally distorts evaluation of the Proposal. As Commissioner Peirce notes in her dissent, the TCFD website openly acknowledges that its framework is designed to "empower[] … the markets to channel investment to sustainable and resilient solutions, opportunities and business models."[52]

[48] The Proposal, p. 368.
[49] It might be that for the U.S., the reference to global standard for sustainability disclosures in the G7 finance ministers' communiqué (quoted above) refers to the Proposal. The implications of this are examined in Section IV below.
[50] SEC, Peirce, "We Are Not the Securities and Environment Commission."
[51] The Proposal, p. 52.
[52] SEC, Peirce, "We Are Not the Securities and Environment Commission."

The TCFD was formed in 2015 under the chairmanship of Michael Bloomberg and worked under the leadership of former Bank of England governor Mark Carney. Both men have been open and honest about its underlying purpose. Indeed, in welcoming the Proposal, Bloomberg said that its adoption would "accelerate the transition to clean energy and net-zero emissions."[53] Carney has also been clear about the purpose of disclosure in driving climate action, tweeting in May 2021: "What gets measured gets managed. That's why reporting climate-related financial info is critical if we are to achieve #netzero."[54]

However, the Proposal almost entirely suppresses evidence of the link between the demand for corporate GHG disclosures and investor-driven corporate GHG reduction targets. For example, the Proposal cites the 2021 Investor Agenda statement on the climate crisis.[55] Yet the Proposal does not mention that the statement talks of the necessity of governments and investors working together to reduce carbon dioxide emissions by 45% by 2030 or investors engaging with companies to cut their emissions.[56] The main exception I found to what otherwise appears to be a systematic exclusion of the link between disclosures and targets is a reference to State Street Global Advisors' 2022 stewardship guidelines on pressing companies to report Scope 1 and 2 GHG emissions and setting targets for emissions reductions.[57]

By contrast, there is abundant evidence that the purpose of GHG emissions disclosures is to drive corporate behaviors and adoption of emissions targets. Welcoming the Proposal, Anne Simpson, former head of board governance and sustainability at CalPERS (the nation's largest pension fund) and currently head of sustainability at Franklin Templeton Investments and a board director of CERES, stated that the challenge of directing private capital to achieve net-zero emissions requires standardized, mandatory, and regulated climate risk disclosures. In turn, these will help investors induce corporate action. "The rising number of shareowner proposals … shows clearly that investors will buttress the SEC's requirements by ensuring companies do not avoid action on carbon pricing and targets," she stated in the *Financial Times*.[58] "Money talks," Simpson says on the Climate Action 100+ website, where she is on the steering committee. "If we can deploy capital and the power of financial markets, we can ensure companies make the transition needed to cap global warming."[59]

The point that disclosures have an underlying, non-investment policy goal was made by Larry Fink, chairman and CEO of BlackRock: "But the goal cannot be transparency for

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[53] TCFD, "Statement of Michael R. Bloomberg on the SEC's Proposed Rules to Enhance and Standardize Climate-Related Disclosures for Investors," Mar. 21, 2021, https://www.fsb-tcfd.org/press/statement-of-michael-r-bloomberg-on-the-secs-proposed-rules-to-enhance-and-standardize-climate-related-disclosures-for-investors.
[54] Mark J. Carney, Twitter, May 20, 2021, https://twitter.com/markjcarney/status/1395824350511648769.
[55] The Proposal, p. 333 & fn. 790.
[56] Investor Agenda, "2021 Global Investor Statement to Governments on the Climate Crisis," Oct. 27, 2021, https://theinvestoragenda.org/wp-content/uploads/2021/09/2021-Global-Investor-Statement-to-Governments-on-the-Climate-Crisis.pdf.
[57] The Proposal, p. 335.
[58] Anne Simpson, "Why the SEC Is Right to Make Climate Risk Disclosure Mandatory," *Financial Times*, Mar. 30, 2022, https://www.ft.com/content/b6cc17f0-c0c3-476a-bb77-1e7c1e9e946a.
[59] https://www.climateaction100.org/business-case.

transparency's sake. **Disclosure should be a means to achieving a more sustainable and inclusive capitalism**," Fink wrote in his 2020 letter to CEOs.[60]

- *It is irrational for the SEC to ignore the intent of the leadership of the TCFD initiative in developing a disclosure regime to act as a corporate decarbonization tool and the evidence that investor demand for TCFD-aligned disclosures is driven by certain investors and climate groups in order to press decarbonization targets on listed companies.*

B. GHG Reduction Targets and Shareholder Value

The principal plank of the Proposal's justification for mandatory GHG emissions disclosure is as a reliable indicator of transition risk, a rationale that the SEC knows to be spurious, for reasons examined in Section IV below. However, the Proposal also deploys three subsidiary reasons:

> *First*, they are fundamental to investors' understanding of a registrant's business;
>
> *Second*, they enable investors to assess and compare registrants' progress in meeting GHG reduction targets; and
>
> *Third*, meeting corporate decarbonization targets incurs costs that investors need to know about.

Analyzing these helps shed light on the "reasonable investor" standard that the Proposal uses to assess matters that should be considered as material and therefore should be disclosed.[61] The analysis suggests a useful test as to whether an investor is reasonable: If the words "climate activist" replace the word "investor," is the sense of a statement in the Proposal maintained or improved? If it is maintained or improved, it indicates that an investor wanting the relevant information would no longer be considered as acting as a reasonable investor but as a climate activist who happens to own or control shares in a company.

1. Climate disclosures as fundamental to the understanding of a registrant's business

The SEC proposes to include climate-related disclosure rules in Regulations S-K and S-X because "the required disclosure is fundamental to investors' understanding the nature of a registrant's business and its operating prospects and financial performance."[62] The point is also made by Commissioner Allison Herren Lee in her statement welcoming the Proposal:

> Greenhouse gas emissions in many respects resemble financial statement disclosures, involving as they do significant estimates and assumptions and providing critically important insight into a company's operations.[63]

This argument is fallacious. GHG emissions are not fundamental to a business's value and prospects; they are unwanted byproducts of a business's creation of value to customers through

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[60] Emphasis in the original. BlackRock, "Larry Fink's 2020 Letter to CEOs: A Fundamental Reshaping of Finance," Jan. 2020, https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter.

[61] Quoting *TSC Industries v. Northway*, the Proposal argues that something should be considered material "if there is a substantial likelihood that a reasonable [investor] would consider it important." The Proposal, p. 174.

[62] The Proposal, p. 55.

[63] SEC, Allison Herren Lee, "Shelter from the Storm: Helping Investors Navigate Climate Change Risk," Mar. 21, 2022, https://www.sec.gov/news/statement/lee-climate-disclosure-20220321.

its provision of products and services to them and its ability to generate financial returns to shareholders by doing so efficiently and competitively and by undertaking innovation, thereby generating value for shareholders. However, GHG emissions data are of very great interest to climate activists' understanding of a business.

2. Assessment and comparison of companies' progress in meeting decarbonization targets

The Proposal argues that GHG emissions disclosures can be used to evaluate progress in meeting corporate net-zero commitments.[64] Comparability and consistency of such disclosures across companies are required to compare companies with their peer group.[65] In a passage in which the "climate activist" replacement test can be used, the SEC argues that despite the increasing prevalence of corporate decarbonization targets,

> monitoring which firms are taking steps to implement them is difficult given the lack of required standardized metrics for progress. Absent such a monitoring device, investors [i.e., climate activists] have insufficient information to gauge the credibility of the targets.[66]

Why is it in the interests of shareholders—as distinct from climate activists—for companies to adopt GHG reduction targets? The SEC observes that some large investment institutions, collectively with trillions of dollars under management, have adopted net-zero targets for their portfolios, but it doesn't explore the motives for their adoption of net-zero targets.[67] Nor does the SEC attempt to explain how a company's stock market valuation might increase by imposing net-zero climate policies on these institutions' investee companies. Are these institutions behaving as reasonable investors, or are they acting as climate activists with multitrillion-dollar stock portfolios?

At one point, the SEC suggests that mandatory disclosures around climate-related targets could be beneficial in signaling "value-enhancing commitments" to investors.[68] As before, the SEC does not suggest how such commitments would boost a registrant's bottom line. In any case, this is an argument against compulsion because it would be in management's and shareholders' interests to voluntarily make and disclose such commitments.

Elsewhere, the Proposal makes the opposite case for mandatory GHG emissions disclosures on the grounds that management is unable to signal value enhancement from adopting GHG reduction targets: if registrants, the SEC argues, incur short-run costs to cut their Scope 1–3 emissions, thereby reducing short-run profitability,

> but are unable to convey to investors that they are meaningfully following through on achieving potential long-term value-enhancing strategies, there could be a disincentive for investors to invest in the firm, thus undermining its value in the long run.[69]

This is a perilous argument for the SEC to make. The SEC implicitly accepts that the costs to firms, and therefore to shareholders, of adopting decarbonization targets are more certain than the putative benefits, which are therefore likely to be injurious to shareholders' interests. Without any empirical evidence, the SEC assumes market failure (long-term

[64] The Proposal, p. 155.
[65] The Proposal, p. 368.
[66] The Proposal, p. 331.
[67] The Proposal, p. 166.
[68] The Proposal, p. 423.
[69] The Proposal, p. 384.

shareholder value from meeting GHG targets exists, but management can't point to it with the result that the market artificially suppresses the share price), so the SEC proposes to substitute its judgment for that of the stock market's.

- *These attempts by the SEC to argue that its proposed GHG disclosure rules are in the interests of shareholders are implausible, contradictory, and unconvincing. By claiming that its judgment is superior to that of the market, the Proposal risks subverting the efficient operation of the capital markets, contrary to the SEC's mandate to maintain fair, orderly, and efficient markets.*

3. GHG disclosures as tools to elicit cost data on meeting GHG reduction targets

Somewhat inconsistently with the foregoing, in other parts of the Proposal, the SEC is more forthcoming in acknowledging that attempting to meet net-zero incurs net costs. Discussing the potential benefits of its climate disclosure proposals, the SEC argues that "investors may gain better insights into a registrant's estimated costs of any operational changes expected to be implemented to achieve emission reduction targets."[70] In its arguments in favor of Scope 3 disclosures—arguments that pertain equally to disclosures of Scope 1 emissions—the SEC says that such disclosures

> would also enable an investor to assess the efficiency and efficacy of the registrant's actions to achieve its target or goal (*e.g.*, by comparing the registrant's expenditures or other investments in lower carbon transition activities from year to year with any corresponding reduction in its Scope 3 emissions).[71]

If a registrant has been incurring little cost in meeting an ambitious target, "these disclosures could indicate to investors that the registrant may need to make a large expenditure or significant change to its business operations."[72]

Noting empirical evidence that mandatory GHG emissions disclosures result in reduced emissions among affected firms, the SEC states that "this could also come with the potential cost of lower productivity, profitability, or market share in the short term."[73] The Proposal doesn't indicate how these short-term costs are more than outweighed by increased profitability over the longer term.[74] Even if the registrant's competitors are forced to cut their emissions, higher costs mean squeezed profit margins and/or a smaller market due to reduced consumer demand.

The foregoing demonstrates that the SEC is fully aware that meeting GHG emissions targets can incur significant cost. Yet the SEC does not examine the motives of investors and investor groups calling for mandatory GHG disclosures. In calling for mandatory GHG disclosures and pressing companies to adopt decarbonization targets, such investors are not

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[70] The Proposal, p. 358.
[71] The Proposal, p. 177.
[72] Ibid.
[73] The Proposal, p. 420.
[74] Elsewhere, the SEC makes the bizarre suggestion that the absence of mandatory GHG emissions disclosures gives short-term-focused managers an incentive to initiate projects exposed to climate risk without informing investors (The Proposal, p. 355). In the real world, the oft-made complaint is that short-term-focused managers forgo projects of potential long-term value in order to increase cash generation and fund, for example, stock buybacks.

behaving as reasonable investors because, as the SEC acknowledges, what they want incurs costs that are likely to be detrimental to shareholders' financial interests. Rather, these investors are acting from nonfinancial motives, principally to help deliver public policy objectives in the form of the Paris climate agreement and the Biden administration's goal of net zero by 2050, in accordance with the doctrines of stakeholder capitalism, as articulated by Fink in his 2020 letter to CEOs quoted above. The SEC's mandate, however, is to protect investors, not stakeholders.

- *Much of the Proposal's justification for mandatory GHG emissions disclosures relies on the argument that what is material is whatever investors deem to be material. It is negligent of the SEC not to have probed the motives of investors who have been pressing the SEC to adopt mandatory GHG emissions disclosures. Unless this is rectified and the SEC demonstrates—contrary to the evidence that it presents in the Proposal—that GHG reduction targets are financially beneficial to registrants, investor representations in favor of mandatory GHG disclosure should be discarded.*

IV. The Proposal's Spurious Climate Transition Risk Justification

The principal defect of the Proposal is that it takes a sustainability disclosure framework designed to cut corporate GHG emissions and shoehorns it into a transition risk justification. It is for this reason that the SEC's various justifications for the Proposal are implausible and unconvincing. The case for other jurisdictions to adopt similar disclosure frameworks—as they are doing—for the purpose of sustainability is beside the point. What matters here is the SEC's proposed use of a sustainability framework for the stated purpose of accurately assessing financial risk, which, in turn, gives rise to the chief benefit that the SEC claims for the Proposal:

> Capital allocation would become more efficient as investors are better able to price climate-related risks.[75]

If, however, the adoption of a sustainability framework as a misleading framework of financial risk, it could give rise to mispricing of risk and misallocation of capital, and the claimed benefit of the Proposal becomes a cost.

When it comes to the SEC's assertion that GHG emissions disclosures would be a tool to enable investors to assess a registrant's exposure to transition risk, it can be demonstrated that the SEC knows this justification to be spurious because such disclosures would be a systematically misleading indicator of risk, as they treat the world as a single, homogenous climate regulatory space. The SEC knows this to be false, as it recognizes that transition risk is jurisdiction-specific:

> A registrant that has significant operations in a jurisdiction that has made a GHG emissions reduction commitment would likely be exposed to transition risks related to the implementation of the commitment.[76]

This is not an isolated example in the Proposal. Here are three more:

- For example, a registrant that operates in a jurisdiction that has imposed, or is likely to impose, limits on GHG emissions in support of the Paris Agreement might set a long-term target of net-zero GHG emissions from its operations in 2050, a medium-term target of reducing its emissions by 30% by 2030, and a

[75] The Proposal, p. 13.
[76] The Proposal, p. 63.

short-term target of maintaining its emissions at its 2020 rate through 2023. This registrant could face material transition risks due to the estimated costs of the operational changes expected to be implemented to achieve these targets.[77]

- Adoption of a transition plan to mitigate or adapt to climate-related risks may be an important part of a registrant's climate-related risk-management strategy, particularly if it operates in a jurisdiction that has made commitments under the Paris Agreement to reduce its GHG emissions.[78]
- A transition plan may include a plan to reduce its GHG emissions in line with a registrant's commitments or commitments of jurisdictions within which it has significant operations.[79]

The Proposal notes that governments around the world have made public commitments to transition to a lower-carbon economy and cites a February 2021 speech by Secretary of State Anthony Blinken on the U.S. rejoining the Paris Agreement.[80] As explained in my November 2021 report "Climate-Risk Disclosure: A Flimsy Pretext for a Green Power Grab," submitted with this letter, the Paris Agreement signaled the abandonment of attempts to solve the climate policy "free-rider" problem—countries that don't cut their emissions gain the climate benefits from those that do—that has bedeviled effective global action on climate for three decades.[81] After the failure of the 2009 Copenhagen climate conference to agree to a climate treaty providing for binding emissions cuts on the parties, the Paris Agreement represents a retreat from multilaterally-agreed GHG emissions targets (e.g., the approach of the 1997 Kyoto Protocol, which, however, excluded the majority of the world's emitters) to unilateral commitments in the form of Nationally Determined Contributions. In this way, the reality of global climate policy fragmented by national jurisdictions is reflected and enshrined in the Paris Agreement.

Even considering jurisdictions that have passed net-zero laws does not automatically translate to laws and regulations that curtail emissions on the time scales implied by national decarbonization commitments. For example, the United Kingdom was one of the first countries to legislate a net-zero objective, but according to the Climate Change Committee, the country is not on track to meet the government's fourth carbon budget (2023–27) or its fifth (2028–32). "To meet future carbon budgets and the Net Zero target for 2050 will require governments to introduce more challenging measures," the committee says.[82] Not only is transition risk jurisdiction-specific; within jurisdictions, it will vary from sector to sector and be dependent on the specific policies and regulations that governments enact in an attempt to meet national decarbonization goals. Inferences about transition risk based on a company's aggregate GHG emissions are therefore very likely to be highly misleading.

Although the SEC acknowledges the reality that climate regulations and, therefore, transition risk are jurisdiction-specific, the Proposal's tabulations of GHG disclosures would not be disaggregated by jurisdiction, thereby creating a systematically misleading indicator of

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[77] The Proposal, pp. 78–79.
[78] The Proposal, p. 108.
[79] The Proposal, p. 109.
[80] The Proposal, p. 12 & fn. 18.
[81] Rupert Darwall, "Climate-Risk Disclosure: A Flimsy Pretext for a Green Power Grab," RealClear Foundation (Nov. 2021), p. 17.
[82] Climate Change Committee website, "Advice on Reducing the UK's Emissions," https://www.theccc.org.uk/about/our-expertise/advice-on-reducing-the-uks-emissions.

climate transition risk. The Proposal goes on to claim that these misleading tabulations will reduce information asymmetries between firms and investors and among investors and reduce the informational advantage of informed traders.[83] Insofar as such disclosures carried weight with investors—especially less sophisticated ones—as proxies for climate transition risk, they would likely worsen informational asymmetries and risk creating a false market in the most affected securities.

- *In order to make the Proposal's GHG emissions disclosure rules comport with the SEC's mandate to protect investors, the SEC asserts that mandating such disclosures is required as indicators of transition risk. This is contradicted by statements in the Proposal that correctly point out that transition risk is jurisdiction-specific, implying that the such disclosure requirements would be contrary to the SEC's mandate to maintain fair, orderly, and efficient markets. However, these disclosure requirements make perfect sense if the objective is to facilitate investors imposing and enforcing decarbonization targets on registrants, thereby revealing the Proposal's real policy motive and its stated one as pretextual.*

The charge that the Proposal's true justification with respect to GHG disclosures is not its stated, pretextual one gains additional support from the Proposal's stated aim of preventing regulatory arbitrage. There are also passages where the Proposal's true motive is more overt—where the Prince appears briefly on stage. Notwithstanding these brief appearances, because the Proposal's motive, like an iceberg, remains mostly submerged, the SEC has not conducted a proper cost-benefit analysis taking account of the likely impact of the proposed GHG emissions disclosure rules.

A. Regulatory Arbitrage and the SEC's Underlying Motive

The ostensible purpose of GHG disclosures is to provide investors with information about registrants' possible exposure to the risk of climate regulations forcing them to cut their GHG emissions. Under the Proposal, disclosure of Scope 1 and 2 emissions is to become mandatory, together with disclosure of Scope 3 emissions if a registrant has a Scope 3 target or its Scope 3 emissions are deemed material. However, only registrants' Scope 1 emissions would be directly regulated. Scope 2 emissions reflect the generating mix of the regional electrical grid and therefore reflect the emissions policies that generators and grid operators are subject to.[84] Scope 3 emissions span those emitted by other parties from a registrant's entire upstream and downstream value chain.

In extending mandatory disclosures to Scope 3 emissions, the question needs to be posed: Is the SEC's real concern to provide investors with information pertaining to the likely impact on a registrant's business of future climate policies, or is it to help investors monitor and enforce corporate decarbonization targets?

Scope 3 emissions can be highly attenuated from a firm. For example, a retailer's Scope 3 emissions include its customers' emissions driving to and from its stores. Without draconian climate policies, including economy-wide carbon pricing forcing up gasoline prices even higher, it is highly improbable that Scope 3 emissions data tell us anything about likely financial impacts on a retailer of future climate policies. Since the failure of the Waxman-

[83] The Proposal, pp. 356–57.
[84] The Proposal has restrictions on the use of Renewable Energy Certificates, which is discussed further in Section VI below.

Markey cap-and-trade bill in 2010, there is no evidence suggesting that Congress is likely to pass comprehensive climate legislation for the foreseeable future. Indeed, efforts such as the SEC's with the Proposal can be viewed as alternatives to climate legislation in order to achieve climate policy objectives, such as the Biden administration's goal of net zero as envisaged by the May 2021 EO.

On the other hand, the Proposal reveals the SEC's true intent in wanting disclosure of Scope 3 emissions. It could, the Proposal says, highlight instances where a registrant outsources carbon-intensive activities so that its Scope 1 and 2 emissions are lower than those of a similar company.

> Thus, Scope 3 emissions reporting could provide greater transparency and help preclude any efforts by registrants to obscure for investors the full magnitude of the climate-related risks associated with their GHG emissions.[85]

In this context, recall again Larry Fink's words about the goal not being transparency for transparency's sake but as a means to achieve a more sustainable and inclusive capitalism. Note, too, the throwaway line about the full magnitude of climate-related risks. The magnitude of the physical risk to a registrant's operations from its GHG emissions, however defined, is infinitesimal.

Later on in the Proposal, the SEC is explicit in seeing the requirement to disclose Scope 3 emissions as a tool to curtail the scope for regulatory arbitrage. It cites a study that shows that a firm's relative share of Scope 1 emissions tends to fall at the expense of a rising proportion of supplier-generated Scope 3 emissions and notes the incentives related to regulatory arbitrage:

> By requiring the disclosure of Scope 3 GHG emissions, the proposed rules would make it more difficult for non-S[mall] R[eporting] C[ompany] registrants to avoid investors' scrutiny by outsourcing all or part of their activities abroad.[86]

Were the SEC genuine in its stated motive for the Proposal about its purpose being to inform investors of regulatory risk, regulatory arbitrage would not be something that it would seek to hinder or even highlight as a problem. Regulatory arbitrage is a permissible means for a company to manage its regulatory risk exposures, just as corporations engage in multi-jurisdictional tax planning to minimize corporate income tax liabilities. But viewed through the prism of climate policy and facilitating investors in pursuing corporate decarbonization policies, Scope 3 emissions disclosures make a great deal of sense in trying to prevent corporations pushing emissions beyond the reach of climate activist investors.

- *However it is wrapped up, the inclusion of mandatory Scope 3 emissions disclosures in the Proposal is driven by climate policy objectives, not the stated one of alerting investors to potential regulatory risk. This demonstrates that the Proposal's motive is pretextual and that the SEC's denial of such a motive is gaslighting.*[87]

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[85] The Proposal, p. 176.
[86] The Proposal, p. 375.
[87] The Proposal, p. 178.

B. Pretextuality and the Absence of a Rigorous Cost-Benefit Analysis

Because the underlying purpose of the Proposal is not the stated one, the SEC has not conducted a cost-benefit analysis of the Proposal based on its real (non-pretextual) policy objective and what the Proposal is likely to do, these being closely linked.

In a January 2022 report for the Institute for Policy Integrity, legal scholars Jack Lienke and Alexander Song note that the SEC is obliged to consider the effects of its regulations on "efficiency, competition, and capital formation," which the U.S. Court of Appeals of the D.C. Circuit has interpreted as requiring a form of cost-benefit analysis. They further note that the same court has vacated or remanded past SEC regulations due to inadequate cost-benefit analysis.[88]

For the purposes of conducting a cost-benefit analysis, SEC internal guidance separates costs into three categories:

- Compliance costs;
- Direct costs, which include "costs arising from intended changes to the behavior of regulated firms"; and
- Indirect costs, which are "costs arising from changes to the behavior of regulated firms or persons beyond those that the rule was intended to achieve," such as distributional and competitive effects and a misallocation of resources resulting from regulatory arbitrage.[89]

Where feasible, the authors note, best practice is to provide a quantitative estimate of a rule's costs and benefits.[90]

1. Cost

In its discussion of potential costs, the Proposal does not follow the SEC's own guidance. Instead of being in a category of its own, compliance costs become the main item under the direct costs heading; and noncompliance costs, in the form of increased litigation risk, is the main item under indirect costs.[91] There is no discussion of the cost effects of likely behavioral changes of registrants as a result of the Proposal facilitating adoption of more and stronger corporate decarbonization targets. Evidently, the SEC would be shooting itself in the foot if it defined the costs of more stringent corporate GHG emissions disclosures and emissions targeting as a direct cost (i.e., an intended outcome of the Proposal) and thereby admit to its pretextual motivation.

The SEC's gaslighting of its pretextual motive goes further, to exclude discussion of these likely behavioral changes by registrants even as an indirect cost (i.e., a likely unintended outcome of the Proposal). As shown above, the SEC acknowledges that meeting decarbonization targets incurs costs to firms and their shareholders.[92] Evidence reviewed earlier strongly indicates that mandatory GHG emissions disclosures will be used by investors to impose more and tighter decarbonization targets and enhance their ability to monitor them.[93]

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[88] Jack Lienke & Alexander Song, "Assessing the Costs and Benefits of Mandatory Climate Risk Disclosure," Institute for Policy Integrity (Jan. 2022), p. i.
[89] Ibid., p. 22.
[90] Ibid., p. ii.
[91] The Proposal, pp. 388 & 405.
[92] Section III.B.3.
[93] Section III.A.

These effects have major negative implications for corporations and for the wider economy, neither of which are addressed by the SEC in the Proposal.

- *The SEC would be acting capriciously were it to proceed with the proposed GHG disclosure rules without first having conducted a comprehensive cost-benefit analysis in line with its own internal guidance that includes discussion of the costs from the likely behavioral changes of registrants.*

The wider economic effects of investor-compelled corporate decarbonization targets, particularly regarding the oil and gas sector, depend on whether there is an economy-wide carbon price or carbon cap. Without one, the effect of these targets is not to reduce demand for hydrocarbon energy and reduce carbon dioxide emissions, but merely to displace the supply of hydrocarbons from companies most exposed to such investor pressure to those less or completely immune from it, the latter category including companies such as Gazprom, Rosneft, Saudi Aramco, and Petróleos de Venezuela. By contrast, with economy-wide carbon pricing or carbon caps, there will be less supply displacement as demand for oil and gas is constrained.

- *In accordance with the SEC's internal guidance, prior to finalizing its proposed GHG disclosure rules, the SEC should conduct an economic analysis of the likely wider economic impacts of the disclosure rules to assess their distributional and competitive effects with and without national carbon pricing or equivalent measures to suppress demand for carbon-intensive products and services.*

2. Benefit

The SEC's proposed transposition of a sustainability disclosure framework as a risk disclosure framework also distorts the SEC's evaluation of the benefits claimed for the Proposal. For example, the SEC says that GHG emissions disclosure can "assist [investors] in understanding the overall risk of their portfolios."[94] Such disclosures can help investors assess the sustainability of their portfolios in terms of their carbon footprint, but, as noted above, they are systematically misleading indicators of transition risk. As such, a claimed benefit of the Proposal becomes a cost. Far from assisting capital-market pricing of risk, by justifying GHG disclosure rules on the basis that they can serve as indicators of climate transition risk, the SEC would be doing the opposite of assisting capital-market pricing by mislabeling a sustainability disclosure as a climate financial risk disclosure, contrary to its market efficiency mandate.

- *The SEC can't have* it both ways and claim to be acting rationally: either the SEC should drop its claim to improved market efficiency as a benefit of the Proposal, or it should remove the GHG disclosure rules from the Proposal.*

C. Direct Evidence of Pretextuality in the Proposal

Although the Proposal's cost-benefit analysis is heavily distorted by the SEC's desire to keep the Proposal's true justification under wraps, there are a few passages where the SEC's real reason for the Proposal is stated in a more or less straightforward manner—most notably, those in Table 3 below.

[94] The Proposal, p. 368.

Table 3: The SEC's Real Rationale—Excerpts from the Proposal

▪ Despite the increasing prevalence in stated [decarbonization] targets and goals, monitoring which firms are taking steps to implement them is difficult given the lack of required recurring standardized metrics for progress. Absent such a monitoring device, investors have insufficient information to gauge the credibility of the targets.[95]
▪ State Street Global Advisors (SSGA) and BlackRock, two of the world's largest investment managers, recently announced the focus areas for their asset stewardship program for 2022, with climate at the top of their priority list. One of the key expectations set by SSGA this year is a requirement for companies to provide disclosures aligned with TCFD recommendations, including reporting on board oversight on climate-related risks and opportunities, Scope 1 and 2 GHG emissions, and targets for emissions reductions.[96]
▪ BlackRock expects to continue encouraging companies to demonstrate that their plans are resilient under likely decarbonization pathways, and to ask that companies disclose a net-zero aligned business plan that is consistent with their business model to demonstrate how their targets are consistent with the long-term economic interests of their shareholders.[97]
▪ As institutional investors and other commenters have indicated, GHG emissions information is important to investment decisions for various reasons, including because GHG emissions data is quantifiable and comparable across industries and can be particularly useful in conducting a transition risk analysis; it can be used to evaluate progress in meeting net-zero commitments and assessing any associated risks; and it may be relevant to investment or voting decisions because GHG emissions could impact the company's access to financing, as well as its ability to reduce its carbon footprint in the face of regulatory, policy, and market constraints.[98]

The rationale for the Proposal's insistence on standardized GHG data is evident from Table 3: to enable investors (in this instance, indistinguishable from climate activists, other than that they own or manage shares) to compare, monitor, and enforce corporate decarbonization targets. It is important to recognize that no jurisdiction in the world has passed legislation forcing companies to achieve net-zero GHG emissions.[99] In the U.S., which has not passed any net-zero climate legislation, this is an investor-led push that the Proposal is designed to support and facilitate.

It is for this reason that the Proposal would require companies to identify individual board members or board committees responsible for the oversight of climate-related risks.[100] The Proposal does not explain the rationale for this requirement. However, the European-based

[95] The Proposal, p. 331.
[96] The Proposal, p. 335.
[97] The Proposal, pp. 335–36.
[98] The Proposal, pp. 154–55.
[99] Under the U.K.'s plans to be the world's first Net Zero–Aligned Financial Centre, announced at the Glasgow climate conference, listed companies will have to publish transition plans that consider the government's net-zero commitment or provide an explanation if they have not done so. The plan will also provide for "strong Government oversight of the financial sector as a whole to ensure financial flows actually shift towards supporting net zero." HM Treasury, "Fact Sheet: Net Zero–Aligned Financial Centre," Nov. 2, 2021, https://www.gov.uk/government/publications/fact-sheet-net-zero-aligned-financial-centre/fact-sheet-net-zero-aligned-financial-centre.
[100] The Proposal, p. 100.

Institutional Investors Group on Climate Change (the "IIGCC"), an organization cited in the Proposal as lobbying for increased disclosure on climate-related risks[101]—"[o]ur mission is to support and enable the investment community in driving significant and real progress by 2030 toward a net-zero and resilient future"[102]—does explain the thinking behind this rule. In a July 2021 statement, the IIGCC said that companies should be required to name a director responsible for the net-zero transition plan.

> This enables investors to determine which Board directors, in addition to the Chair, should be engaged with and potentially (as a last resort) voted against when a plan has not been provided or implementation is insufficient.[103]

The IIGCC made no pretense that these requirements have anything to do with maximizing shareholder returns or protecting long-term business value. Indeed, the words "value" and "return" are not mentioned in the IIGCC statement. It is about climate policy enforced by institutional investors. In the words of Yo Takatsuki, J. P. Morgan Asset Management's EMEA Head of Investment Stewardship:

> If we stand any chance of closing the gap between current carbon emissions and meeting the goals of the Paris Agreement, the transition to net zero has to be scientifically credible. Responsibility, accountability and delivery of a credible net zero transition plan, coupled with the provision of good quality data, must therefore be implemented by the Board of investee companies.[104]

- ➢ *In finalizing the Proposal, the SEC has a choice: it can come clean about the underlying purpose of the Proposal and take its chances that Congress gave it the authority to regulate corporate GHG disclosures for this purpose; or it can persist with its pretextual strategy and run with a risk-disclosure justification that would place the SEC in conflict with its mandate to maintain fair, orderly, and efficient markets owing to the fact that corporate GHG emissions data are systematically misleading indicators of climate financial risk.*

V. Climate Risk—In the Eye of the Beholder

The weakness with climate financial risk as a concept is its indeterminateness: it does not represent a category of knowable facts that, once put into the public domain, reasonable people can agree on their implications for investors. Rather, it belongs in a category of what economist John Kay and the former governor of the Bank of England, Mervyn King, in their book of the same title, call "radical uncertainty":

> a situation in which we cannot enumerate a list of all possible future outcomes to which we can then attach probabilities…. They reflect unique situations in which we know something, but not enough to attach probabilities to a well-defined set of future outcomes.[105]

Rather than being inherent in the concept of climate financial risk, the Proposal argues that uncertainty and unknowability reflect shortcomings of current disclosure requirements. "Under the current regime, many climate-related risks may be unobservable or obfuscated,"

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[101] The Proposal, fn. 799.
[102] https://www.iigcc.org.
[103] Quoted in Darwall, "Climate-Risk Disclosure," p. 19.
[104] Ibid.
[105] John Kay & Mervyn King, *Radical Uncertainty: Decision-Making for an Unknowable Future* (New York: W. W. Norton, 2021), p. xv.

the SEC claims, as if changing disclosure rules will magically make the unobservable visible.[106] Elsewhere, the SEC argues that

> the complexity, uncertainty, and long-term nature of climate risks make it unlikely that voluntary disclosure of such risks would be fully revealing.[107]

This line of thinking is tantamount to implying that companies have a file of climate risks that managements keep under lock and key (owing to the difference in incentives between agents and principals) that requires compulsion to be disclosed, so that the risks are then revealed to the public. It is the regulatory equivalent of medieval alchemy and its claim of being able to transmute the dross of current disclosures into the Proposal's gold.

The reality is different. Once past the division between climate physical risk and climate transition risk, the concept of climate financial risk is too nebulous to have practical utility as a stable regulatory principle. Reasonable people can disagree both on what facts constitute climate risk and their implications for business and investors.

Indeed, in the Proposal, we find the SEC disagreeing with itself on a climate risk "fact" and its implications for investors. Thus, on page 67 of the Proposal, the SEC touts opportunities from decarbonization "such as cost savings associated with the increased use of renewable energy." Twelve pages later, in a discussion on the implications for a registrant from reducing its Scope 1 and 2 emissions, the Proposal states that these could involve increased expenses in the short term, related to "increasing the amount of electricity purchasing electricity from renewable sources."[108] If the SEC is confused about whether an identical climate risk is positive or negative for a business, how can it expect registrants to accurately disclose and characterize such risks, especially when they have the added burden of litigation risk?

Moreover, climate is a deeply politicized field where "facts" can turn out to be wrong or misused to create highly misleading inferences about climate change. A case in point is the National Oceanic and Atmospheric Administration's ("NOAA") Billion Dollar Climate and Weather data set and its claim that 2020 saw a record 22 separate climate-related disasters with at least $1 billion in damages, which is cited in the Proposal.[109] Presumably, the intent of including this statement in the Proposal is to demonstrate the worsening impact of climate change. If so, it could be classified as climate misinformation.

In July 2021 testimony to the Senate Committee on Banking, Housing, and Urban Affairs, Roger Pielke, Jr., a professor of environmental studies at the University of Colorado–Boulder, showed why this inference would be misleading. Data and evidence indicate that since at least 1990 (about when global data on disaster losses are judged to have become reliable), the economic damages associated with extreme weather have decreased when measured in the context of global GDP. Pielke criticized NOAA for its billion-dollar data set:

> What the dataset actually shows is a combination of poor methodology and the consequences of a growing society, with more people and property in locations exposed to loss from extreme weather. It is not an indicator of climate change. Climate data, not economic data, should be used for that purpose.[110]

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[106] The Proposal, p. 355.
[107] The Proposal, p. 410.
[108] The Proposal, p. 79.
[109] The Proposal, fn. 10.
[110] Quoted in Darwall, "Climate-Risk Disclosure," p. 13.

Thanks to NOAA's sleight-of-hand methodology, a $600 million hurricane in 1985 (Hurricane Kate) would have been about a $2 billion hurricane in 2021 but is not included in NOAA's data set. As Pielke testified:

> Every time you see this dataset invoked as evidence of human caused climate change you should think instead about the state of scientific integrity in U.S. federal science agencies.[111]

Pielke's observation illustrates the risk that the SEC is incurring in allowing itself to be used as a tool of politicized science.

- *The Proposal would require registrants to identify management positions and committees responsible for assessing and managing climate-related risk and the relevant expertise of such position holders.*[112] *Yet the Proposal demonstrates the SEC's own deficiency of the level of climate knowledge that it expects of commercial firms and demonstrates that it lacks the necessary objectivity to assess registrants' climate-related filings and bears out Commissioner Peirce's observation that the SEC does not have the expertise to act as a Securities and Environment Commission.*[113]

A. Climate Physical Risk

The premise of the Proposal's discussion of climate physical risk is that climate change already has, or will shortly have, a material impact on registrants' operations. With the partial exception of exposure to the risk of wildfire, particularly in California, the case developed in the Proposal is notable for its thinness. SEC staff keyword analysis of filings reveals that "the majority of the disclosure is focused on transition risks, with comparatively fewer mentions of physical risk."[114] This is borne out by data on climate-related keywords by sector, which show that agriculture, with one of the highest exposures to the physical climate (i.e., weather), is ranked halfway down (17 out of 34) in filings with climate-related keywords.[115]

Moreover, its treatment of the threat posed by climate physical risk is unbalanced, insofar as it excludes countervailing evidence and analysis. For example, the Proposal does not mention a November 2021 paper by staff at the New York Fed, "How Bad Are Weather Disasters for Banks?" To which the authors answer:

> Not very. We find that FEMA disasters over the last quarter century had insignificant or small effects on U.S. banks' performance. This stability seems endogenous rather than a mere reflection of federal aid. Disasters increase loan demand, which offsets losses and actually boosts profits at larger banks. Local banks tend to avoid mortgage lending where floods are more common than official flood maps would predict, suggesting that local knowledge may also mitigate disaster impacts.[116]

In mounting a case for its intrusive and detailed disclosures on climate physical risk (down to the last 1% of expenditure and the last zip code!), the SEC's biggest problem is with

[111] Ibid.
[112] The Proposal, pp. 101–2.
[113] SEC, Peirce, "We Are Not the Securities and Environment Commission."
[114] The Proposal, p. 321.
[115] The Proposal, table 3.
[116] Kristian S. Blickle, Sarah N. Hamerling, and Donald P. Morgan, "How Bad Are Weather Disasters for Banks?" *Federal Reserve Bank of New York Staff Reports*, no. 990 (Nov. 2021; rev. Jan. 2022).

the science of climate change. In a June 2021 presentation to the U.S. Federal Energy Regulatory Commission, the climatologist Judith Curry addressed the science behind climate change and extreme weather events:

> Apart from the reduced frequency of the coldest temperatures, the signal of global warming in the statistics of extreme weather events remains much smaller than that from natural climate variability, and is expected to remain so at least until the second half of the 21st century. Rather than focusing on the relatively small and uncertain impacts of global warming on extreme events, a broader range of extreme weather events from the historical record can provide a better basis for avoiding "big surprises."[117]

It is unsurprising, therefore, that the Proposal conflates physical climate risk with weather risk and labels it climate-related events. So the SEC is proposing that registrants be required to itemize spending arising from "severe weather events and natural conditions, and the identified physical risks (collectively 'climate-related events')," these to include "[e]xtreme temperatures," i.e., extreme low as well as extreme high temperatures.[118] Given that the SEC accepts that climate physical risk is a subset of weather risk (albeit rebranding the latter as climate), the question the SEC doesn't answer is: What physical and financial evidence from severe weather events can the SEC point to that impels it to propose highly detailed and burdensome disclosure requirements on how much registrants spend on protecting their assets from weather and how much bad weather might cost the business in any one year?

Severe weather is not a recent phenomenon in the United States. Referring to the dust bowl of the 1930s, climate scientist Siegfried Schubert of the NASA Goddard Space Flight Center described the 1930s drought as "the major climatic event in the nation's history."[119] The dust bowl coincided with the establishment of the SEC. Yet only now, after nearly nine decades of its existence—a period when the U.S. economy became increasingly resilient against extreme weather—does the SEC decide that a vastly detailed disclosure regime on weather expenses and the location of assets potentially exposed to bad weather is necessary. Why? One thing is clear. It's not impelled by objective data.

- *The extent of the detail required by the proposed disclosure rule on weather/climate-related expenses and asset location is absurd and unjustified, and, in the absence of a compelling justification, it would be irrational for the SEC to proceed with it.*

B. Climate Transition Risk

Presumption also marks the SEC's approach to climate transition risk: there is an energy transition under way, and companies that fail to conform to it will be negatively affected. But, as with physical climate risk, there is little evidence to back it up other than expressions of aspiration. This presumption is evident in the Proposal's justification for disclosure of Scope 3 emissions. Registrants with high Scope 3 emissions, it is suggested, could be more likely to face disruption to their business models and cash flows. If consumer demand changes to favor less carbon-intensive products,

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117 Quoted in Darwall, "Climate-Risk Disclosure," p. 15.
118 The Proposal, p. 124.
119 NASA, "NASA Explains 'Dust Bowl' Drought," Mar. 18, 2004, https://www.nasa.gov/centers/goddard/news/topstory/2004/0319dustbowl.html.

> companies with high Scope 3 emissions may see a market reduction in demand for their products, and companies that are not aware of these risks could be less profitable relative to those that understand these risks and are prepared to mitigate them.[120]

Here, the SEC indulges in speculation without a shred of evidence, even though there is no shortage of evidence. The SEC's problem is that the evidence does not support the SEC's presumption. The experience of climate policy is how difficult it is to reduce reliance on hydrocarbons; a major factor in the reduction of U.S. emissions in the power sector is the switch from one hydrocarbon (coal) to another (natural gas).

In a 2007 paper, Cass Sunstein, at the time a law professor at the University of Chicago, analyzed the various responses to the threat of ozone depletion from chlorofluorocarbons (CFCs) and of climate change from greenhouse gases and the success of the Montreal Protocol designed to address the former and the failure of the Kyoto Protocol to bend the global emissions curve of the latter. In his analysis, Sunstein noted how consumers spontaneously cut their purchases of CFCs:

> In a brief period, American consumers responded to warnings by cutting their demand for aerosol sprays by more than half, thus dramatically affecting the market. The same public concern spurred domestic regulation. In 1977, Congress amended the Clean Air Act to permit the Administrator of EPA to regulate "any substance ... which in his judgment may reasonably be anticipated to affect the stratosphere, especially ozone in the stratosphere, if such effect may reasonably be anticipated to endanger public health or welfare."[121]

The change in consumer behavior was not extremely burdensome to consumers, Sunstein observed. Aerosol spray cans are not central to daily life, and a refusal to purchase them, or a decision to take other steps to reduce uses of ozone-depleting chemicals, did not impose large costs.[122]

The response of consumers to the threat of climate change caused by combustion of fossil fuels has been very different. Despite 17 years of media attention on climate change,

> the public has yet to respond to that attention through consumer choices, and the best evidence suggests that American citizens are not, in fact, greatly concerned about the risks associated with warmer climates. Notwithstanding the publicity given to climate change in recent years, Americans recently ranked the environment twelfth on a list of the most important problems—below immigration, health care, and gas and heating oil prices.[123]

In the intervening decade and a half, media and political attention on climate change has intensified still further, as has the language used to describe it. In spite of this, demand for oil in the U.S. remained more or less flat for the decade, until the pandemic struck. As it turned out, 2007 was the peak year for oil consumption before the financial crash, when demand fell by 4.6%. By the pre-pandemic year of 2019, demand had inched up 1.8% on 2008—numbers that provide little support for the SEC's presumption that consumers are shunning, or are likely to shun, carbon-intensive energy over fears of climate change. Moreover, oil is a global market,

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[120] The Proposal, p. 374.
[121] Cass R. Sunstein, "Of Montreal and Kyoto: A Tale of Two Protocols," *Harvard Environmental Law Review* 31 (2007): 11.
[122] Ibid.
[123] Ibid., 45.

and U.S. oil companies' revenues and profitability are determined largely by global demand and supply. As shown in Table 4, global demand for oil has grown strongly since the global financial crisis, meaning that the U.S. market has shrunk in relative importance.

Table 4: U.S. and Global Consumption of Oil and Petroleum Liquids (thousands of barrels of oil per day)

	2007	2008	*Change*	2019	*Change*
United States	15,820	15,094	*–4.6%*	15,367	*+1.8%*
World	87,106	86,515	*–0.7%*	100,369	*+16.0%*

Source: Energy Information Authority (U.S.); BP Statistical Review of World Energy, 2018 and 2021 (world)

The presumption that oil demand and prices are in structural decline is a thread running through the Proposal. In its discussion of climate-related risks, the Proposal speaks of the risks to investors associated with a "potential" transition to a less carbon-intensive economy and "long-term shifts in market prices."[124] In the Proposal's discussion of disclosures regarding climate-related impacts on strategy, business model, and outlook, the SEC suggests that "[a]n oil company might discuss a change in the valuation of its proven reserves because of an anticipated reduced demand for fossil fuels."[125]

It is not the job of the SEC to put its thumb on the scales of market developments. Moreover, its prognostications on the energy market are especially ill-timed, with soaring gasoline prices becoming a top concern shared by voters and the Biden administration. During the comment period on the Proposal, it was reported that President Biden was planning a trip to the Kingdom of Saudi Arabia, which, according to Reuters, "would be aimed at bolstering relations with Saudi Arabia at a time when Biden is trying to find ways to lower gasoline prices in the United States."[126] At this year's CERAWeek energy conference in March, Secretary of Energy Jennifer Granholm called on energy companies to raise output. "I hope your investors are saying these words to you as well: In this moment of crisis, we need more supply…. Right now, we need oil and gas production to rise to meet current demand," she told energy executives in the audience.[127]

- *The Biden administration's response to soaring oil prices illustrates the danger for the SEC when it puts itself in the position of engaging in climate and energy policy. Strip away the Proposal's pretextual justification, and one of the chief aims of the Proposal is to give investors and climate activists enhanced leverage over U.S. listed energy companies and the financial institutions that fund them to throttle investment in oil and gas production, contrary to what the Secretary of Energy is telling investors.*

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[124] The Proposal, pp. 59–60.
[125] The Proposal, pp. 80–81.
[126] Andrea Shalal & Steve Holland, "Biden Opens Door to Possible Trip to Saudi Arabia," Reuters, June 3, 2022, https://www.reuters.com/world/middle-east/biden-opens-door-possible-trip-saudi-arabia-2022-06-03.
[127] Pippa Stevens, "U.S. Energy Secretary Granholm Calls on Oil and Gas Companies to Raise Output," CNBC, Mar. 9, 2022, https://www.cnbc.com/2022/03/09/us-energy-secretary-granholm-calls-on-oil-and-gas-companies-to-raise-output.html.

C. Uncertainty and the Proposal's Overly Prescriptive Disclosure Requirements

The concept of climate transition risk set out in the Proposal embodies a deterministic view of the future: that the future is foreseeable and has been foreseen. This view of the SEC subverts the function of capital markets, which is to embody divergent, sometimes contradictory, views about the future in the prices of securities. In keeping with this view, the SEC is proposing highly rigid disclosure requirements, to the extent of determining the denominators that registrants must use for carbon intensity metrics, thereby foreclosing spontaneous market-led disclosures that might serve investors better. Indeed, with respect to physical risks, the Proposal acknowledges "the uncertainty surrounding the future path of climate change and the evolving nature of the science and methodologies measuring their economic impacts" but perversely sees this as a justification for the Proposal's highly prescriptive approach.[128]

The inclusion of a proposed requirement for registrants to disclose Scope 3 emissions is also questionable. In addition to Scope 3 disclosures being motivated as a tool of climate policy (Section IV.A above), there is a fundamental problem with the concept and methodology of Scope 3 emissions. "Although Scope 3 emissions can constitute a large proportion of a registrant's total emission," the Proposal explains their exclusion from attestation requirements "due to the unique challenges associated with their measurement, which is based on data sources not owned by the registrant."[129] This statement needs careful parsing. The fundamental characteristic of Scope 3 emissions is that they are *not* the registrant's emissions; they are someone else's and are therefore not part of a registrant's total emissions.

There is a more fundamental conceptual problem with Scope 3 emissions. Adding up all firms' Scope 1 emissions would equal the total of those firms' emissions. Scope 3 emissions are different. The methodology doesn't comply with the accounting principle that one party's credit is another party's debit. It does not have the rational methodology of value-added taxes, where firms' input taxes are deducted from their output tax, which is levied along the value chain to the final consumer. The outcome of the Scope 3 methodology is that the same emission is counted many, many times over. Aggregating Scope 3 emissions therefore results in a meaningless number that does not reflect any physical reality.

Neither would Scope 3 emissions disclosures deepen investor understanding. For example, the SEC says that the climate transition raises financial risk for automobile manufacturers (it does) and that investors can use Scope 3 emissions data to assess whether a particular auto manufacturer is taking steps to mitigate, or adapt to, the risks posed by the transition to lower-emissions vehicles.[130] Corporate Average Fuel Economy ("CAFE") and other emissions standards are applied to automakers' new car range by model year, based on vehicles' wheelbase, the latest standards being for model years 2024–26, whereas Scope 3 disclosures include emissions from downstream activities for the mileage clocked up by every vehicle sold, not just new vehicles sold in a particular year.[131] Vehicles must meet relevant emissions standards or they cannot be sold. Investors will learn far more about an auto

[128] The Proposal, p. 345.
[129] The Proposal, pp. 377–78.
[130] The Proposal, p. 173.
[131] Alix Partners, "It's Time for Vehicle Manufacturers to Shift Gear on Scope 3 Emissions," Oct. 26, 2021, https://blog.alixpartners.com/post/102h99m/its-time-for-vehicle-manufacturers-to-shift-gear-on-scope-3-emissions?news#utm_source=Mondaq&utm_medium=syndication&utm_campaign=LinkedIn-integration.

manufacturer's success in meeting emissions regulations from new sales data than they can possibly infer from Scope 3 emissions data.

- *Mandatory Scope 3 disclosures serve no purpose other than as a blunt instrument of investor-driven decarbonization that should have no place in an SEC rule.*

VI. Reporting Hygiene—Carbon Offsets and Renewable Electricity Certificates

There is a case for updating the SEC's 2010 guidance in light of subsequent developments. Notable ones are the increasing use by companies of carbon offsets and Renewable Energy Certificates ("RECs"). On carbon offsets, Mark Carney commented that companies targeting net zero would need them. Such companies will be seeking to reduce emissions, he said in December 2020,

> but for a period of time, they will also need the "net" in net zero, and they can only get that from a credible global market that needs to be developed.[132]

Regarding RECs, according to the RE100 Climate Group website, more than 370 companies have made a commitment to go "100% renewable" (the quotation marks are from the RE100 Climate Group website). "To achieve 100% renewable electricity, companies must match 100% of the electricity used across their global operations with electricity produced from renewable sources," the operative word in this sentence being "match."[133]

Carney reckoned that the "net" in net-zero requirement would give rise to a \$50–\$100bn/year carbon offset market but acknowledged that there were also issues with verification and greenwashing. The RE100 claim of 100% renewable electricity relies on the use of RECs and an exceedingly loose definition of what constitutes an electricity market. For example, it considers the U.S. and Canada to be a single market for renewable electricity sourcing and reporting.[134] Furthermore, the unique physical property of electricity is that it must be produced the moment it is consumed. The use of RECs, however, depends on the fraudulent—but legal—accounting assumption that renewable electricity is stored.

IBM is one of the very few corporations that is honest and transparent about its approach to accounting for its use of renewable electricity. "There is a difference between purchasing RECs and actually using renewable electricity," IBM says in its 2017 Environment Report:

> A complete understanding of a company's use of renewable electricity requires a high degree of transparency in how renewable electricity and REC purchases are reported. IBM supports and exercises full transparency in disclosing its use of renewable electricity.[135]

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[132] Leslie Hook & Patrick Temple-West, "Carney Calls for '\$100bn a Year' Global Carbon Offset Market," ft.com, Dec. 3, 2020, https://www.ft.com/content/8ed608b2-25c8-48d2-9653-c447adbd538f.
[133] RE100 Climate Group, https://www.there100.org/technical-guidance.
[134] RE100 Climate Group, "Market Boundary for Making Corporate Renewable Electricity Uses Claims," May 27, 2019, https://www.there100.org/sites/re100/files/2020-10/Note%20on%20Market%20Boundaries.pdf.
[135] IBM, "2017 IBM and the Environment Report," June 2018, p. 21.

IBM disavows the purchase of unbundled RECs to offset its consumption of electricity generated from fossil fuels.[136] Unlike the vast majority of corporations' claims on renewable electricity, IBM's reporting transparency extends to identifying electricity consumption where renewable electricity is generated in the same grid region and, crucially, the exact time when renewable generation and IBM's consumption coincide. Without such reporting protocols, the purchase of unbundled RECs is a deceptive accounting mechanism for companies that do not physically consume the renewable electricity that they claim they do.

- *The Proposal's rules that would require registrants to disclose the role carbon offsets or RECs play in the registrant's climate-related business strategy are a welcome first step to improving the reporting hygiene of this murky area of corporate disclosure.*[137]

VII. Conclusion

This letter demonstrates that the Proposal's purpose is pretextual. The SEC has not provided evidence on the inadequacy of existing climate disclosure obligations; it proposes to use a sustainability framework designed to assist investors to impose GHG targets on companies, but denies that this is the purpose behind the Proposal, even though this objective also accords with the climate policies of the Biden administration and those in other jurisdictions using a similar disclosure framework; it relies heavily on investor representations, but fails to probe the motivations and intent behind those representations; it dresses up a sustainability disclosure framework as a climate financial risk one, despite the SEC having reason to know that GHG disclosures are a systematically misleading indicator of climate transition risk; and the inherently indeterminate nature of climate financial risk leads the SEC to commit errors that undermine its standing to adjudicate its proposed disclosure rules. The Proposal makes sense only in terms of what it expressly denies: the Proposal is contemplated as a climate rule to better enable investors and climate activists to impose, monitor and enforce corporate GHG reduction targets.

There is a short version. If it looks like a duck, swims like a duck, and quacks like a duck, then it probably is a duck.

The Proposal is a duck.

Yours sincerely,

Rupert Darwall
Senior Fellow, RealClear Foundation

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[136] IBM, "Renewable Electricity Consumption," https://www.ibm.com/ibm/environment/climate/renewable_energy.shtml.
[137] The Proposal, p. 82.